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March 21, 2016

REDACTED – FOR PUBLIC INSPECTION

By ECFS

Ms. Marlene Dortch
Secretary
Federal Communications Commission
455 12th Street, SW
Washington, DC 20554

Re: WC Docket No. 05-25; RM-10593

Dear Ms. Dortch:

On March 17, 2016, Frank Simone, Keith Krom, Ola Oyefusi, Caroline Van Wie, and the undersigned met with the following Commission Staff: Pam Arluk, William Keyhoe, Christopher Koves, William Layton, Virginia Metallo, Thom Parisi, Joseph Price, Eric Ralph (via telephone), Deena Shetler, and Shane Taylor. We discussed the PowerPoint deck attached hereto as "Attachment A," which summarizes AT&T's pleadings and the expert testimony submitted in this proceeding. In addition, AT&T responded to questions raised by Commission Staff related to a variety of arguments made by certain CLECs in this proceeding. In this letter, we summarize and provide additional detail in response to those inquiries, which relate to (1) whether AT&T has headroom under the current price caps; (2) the number of competitors necessary for effective competition; (3) cable company competitors' impact on AT&T; (4) the ability of CLECs to build lateral connections to buildings; (5) whether an analysis of the special access data collection focused on pricing is necessary or feasible; (6) the ability of CLECs to gain regulated access to ILEC conduit space; and (7) what specific steps the Commission should take in response to the comments submitted in the docket.

1. Headroom Under the Caps. Commission Staff indicated that it believed that AT&T does not have headroom under its special access price caps in Phase I and "no relief" areas, and asked whether such a lack of headroom implies that AT&T has market power because it is not reducing prices in response to competition to levels below the price caps. The answer is obviously no. To begin with, it is not true that AT&T lacks headroom under the special access

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price caps. AT&T today has more than **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** in headroom under its special access price caps.

But even if AT&T had no headroom under the caps, that fact alone would in no way raise any competitive issues. A lack of headroom could be an issue only if the price caps were set above just and reasonable levels. There is no evidence in the record that the current price caps are "too high." To the contrary, the current price caps are presumed to be just and reasonable under Section 201 of the Act pursuant to the Commission's existing incentive regulation scheme,[1] and there are a host of reasons to believe that the Commission's policies have driven the price caps considerably *below* competitive levels.

The Commission adopted the price cap regime for ILECs in 1990 to replace the prior, cost-based, rate-of-return regime. The Commission initialized the first price caps based on the rates permitted under the prior rate-of-return regime as of July 1, 1990,[2] which in turn were based on ILEC costs plus an 11.25 percent rate of return.[3] The evidence in this record indicates that this 11.25 percent rate-of-return was clearly below competitive levels. Indeed, the CLECs have argued that they require a rate-of-return substantially higher than 11.25 percent to remain viable in the marketplace.[4] Thus, the evidence in this proceeding indicates that the price caps were initially set well below competitive levels.

The Commission also adopted X-Factors that first ratcheted down the price caps by 5.3 percent each year until 1997, and then by 6.5 percent per year through July 2004 for special access. As the Commission is well aware, both the D.C. Circuit and the Fifth Circuit found the increased 6.5 percent X-Factor to be "arbitrary and capricious because the FCC did not provide

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[1] Notice of Proposed Rulemaking, *Comprehensive Review of the Part 32 Uniform System of Accounts*, 29 FCC Rcd. 10638, at ¶ 6 (2014) ("Price cap regulation is a form of incentive regulation that relies on a series of Price Cap Indexes (PCIs) to limit the prices carriers charge for services to levels that are *presumed to be just and reasonable*.") (emphasis added).

[2] Second Report and Order, *Policy and Rules Concerning Rates for Dominant Carriers*, 5 FCC Rcd. 6786, Appendix F (1990).

[3] Fourth Further Notice of Proposed Rulemaking, *Price Cap Performance for Local Exchange Carriers*, 10 FCC Rcd. 13659, at ¶ 78 (FCC 1995) ("The rate of return of 11.25 percent is the rate of return adopted in the Re-prescription Order in 1990 for rate-of-return carriers and used to initialize price cap rates.").

[4] *See, e.g.*, Comments of XO Communications, LLC, *Special Access for Price Cap Local Exchange Carriers*, WC Docket No. 05-25, RM-10593 (Jan. 27, 2016) ("XO Comments"), attached Declaration of James A. Anderson, ¶ 22.

sufficient evidence of increased productivity by the LECs to warrant the 6.5 percent figure."[5] But the Commission never corrected that error; the 6.5 percent X-Factor applied each year until 1999. In 2000, the Commission designated a separate basket for special access and ratcheted down those caps by three percent in 2000, and then by 6.5 percent per year from 2001 through 2003.[6] Beginning in July, 2004, the special access price caps were frozen at 2004 levels.[7] Accordingly, for the last decade, the Commission has not even allowed the price caps to increase with inflation, even though there has been substantial inflation during that time (about 26 percent according the Bureau of Labor Statistics).[8] Thus, in real, inflation-adjusted terms, the price caps have effectively fallen substantially since 2004, which means that, in real terms, ILEC special access prices have fallen substantially as well.

In short, the Commission has long recognized that markets are better arbiters of pricing than price regulation regimes. That is particularly true in the special access world, where, after unsuccessful attempts to justify components of the price cap regime, the Commission simply threw its hands up and froze price cap indices more than a decade ago. To draw *any* conclusions about competition from the relationship of market rates to these indices is to give undue credence to an inherently flawed ratemaking mechanism. Consequently, there is no basis on this record to reconsider the price cap levels, and there would never be any grounds to infer market power merely because an ILEC is pricing its services at the cap with no headroom.[9]

2. Existence of One Competitor. The FCC also asked whether the existence of a single competitor is sufficient to ensure competitive outcomes for purposes of these rules. The answer is clearly yes, as has been recognized by the Commission, the Justice Department, and federal courts, and as the economic testimony in this proceeding confirms.

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[5] *Tex. Office of Pub. Util. Counsel* v. *FCC*, 265 F.3d 313, 319 (5th Cir. 2001); *United States Tel. Ass'n* v. *FCC*, 188 F.3d 521 (D.C. Cir. 1999).

[6] Report and Order and Further Notice of Proposed Rulemaking, *AT&T Corporation Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access*, 27 FCC Rcd. 16318, at ¶ 6 (2012).

[7] *Id*.

[8] *See* United States Department of Labor Statistics, Databases, Tables & Calculators by Subject, http://www.bls.gov/data/inflation_calculator.htm.

[9] In addition, the price caps are adjusted each year to reflect exogenous adjustments, and thus headroom can fluctuate from year to year depending on the nature and magnitude of those adjustments. As a result, the existence or non-existence of headroom *in any given year* may simply reflect the nature of the exogenous adjustments in that year; it does not necessarily mean that the ILEC has not been reducing DS1 and DS3 prices.

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In the original *Pricing Flexibility Order*,[10] the Commission based its pricing flexibility triggers on the extent to which CLECs had collocated facilities in ILEC wire centers. For Phase I relief, the ILEC was required to show collocation in at least 15 percent of wire centers within the MSA, or in wire centers accounting for at least 30 percent of revenues for the services in question.[11] For Phase II relief, the ILEC was required to show collocation in 50 percent of wire centers within the MSA, or in wire centers accounting for at least 65 percent of revenues for the services in question.[12] Importantly, however, the Commission found that collocation by multiple CLECs within a wire center was not required. Instead, the petitioning ILEC was required to show only that "that *at least one* competitor relies on transport facilities provided by a transport provider other than the incumbent at each wire center listed in the incumbent's pricing flexibility petition as the site of an operational collocation agreement."[13]

As part of its grant of pricing flexibility, the Commission stressed that the presence of significant sunk facilities by even one competitor was sufficient to prevent the incumbent from engaging in anticompetitive behavior. The Commission explained:

> If *a competitive LEC* has made a substantial sunk investment in equipment, that equipment remains available and capable of providing service in competition with the incumbent, even if the incumbent succeeds in driving that competitor from the market. Another firm can buy the facilities at a price that reflects expected future earnings, and, as long as it can charge a price that covers average variable cost, will be able to compete with the incumbent LEC . . . . [T]he presence of facilities-based competition with significant sunk investment makes exclusionary behavior highly unlikely to succeed.[14]

The D.C. Circuit agreed with this reasoning. It explained that "the presence of facilities-based competition with significant sunk investment makes exclusionary pricing behavior costly

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[10] Fifth Report and Order and Further Notice of Proposed Rulemaking, *Access Charge Reform; Price Cap Performance Review for Local Exchange Carriers*, 14 FCC Rcd. 14221 (1999) ("*Pricing Flexibility Order*").

[11] *Id*. ¶ 93.

[12] *Id*. ¶¶ 148-49.

[13] *Id*. ¶ 82.

[14] *Id*. ¶ 80.

and highly unlikely to succeed," because "that equipment remains available and capable of providing service in competition with the incumbent, even if the incumbent succeeds in driving that competitor from the market."[15]

This analysis is consistent with the Department of Justice's approach in merger cases, where it has also concluded that the presence of a single competitor is sufficient to make the threat of anticompetitive harm unlikely. In prior AT&T and Verizon Consent Decrees, the Justice Department found that the potential for competitive harm existed only in buildings where only "AT&T and SBC or MCI and Verizon, respectively, were capable of supplying local private lines before the merger and *no other competitive LEC* was likely to connect the building to its network."[16] In identifying buildings where divestiture was required, the DOJ began by identifying buildings in the SBC and Verizon territories where the merger would reduce the number of competitors with direct connections (or laterals) "*from two to one*."[17] DOJ then developed "demand/distance 'screens'" to identify whether competitive entry was likely at each "two-to-one building," and DOJ required divestiture only at "two-to-one" buildings where entry by another competitor was found to be unlikely.[18] In buildings where even one additional competitor was actually present, or could reasonably be expected to compete, DOJ found that the likelihood of anticompetitive harm was "unlikely."[19]

These points are further confirmed by the economic testimony. As Professors Israel, Rubinfeld, and Woroch have explained, "[a]s a matter of economics, price cap regulation is unnecessary and is, in fact, counterproductive in areas where rivals have deployed competing facilities-based networks."[20] They have further emphasized that, as a matter of economics, the *first* competitor would have the largest competitive impact, with additional competitors having

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[15] *WorldCom, Inc.* v. *FCC*, 238 F.3d 449, 458-59 (D.C. Cir. 2001).

[16] Memorandum Opinion and Order, *AT&T Inc. and BellSouth Corp., Application for Transfer of Control*, 22 FCC Rcd. 566, at ¶¶ 41-42 (2007) (emphasis added) (discussing the consent decrees).

[17] *Id*. (emphasis added).

[18] *Id*.

[19] *Id*.

[20] Mark Israel, Daniel Rubinfeld, and Glenn Woroch, Competitive Analysis of the FCC's Special Access Data Collection, at 13, filed in WC Docket No. 05-25 (Jan. 27, 2013) ("Israel-Rubinfeld-Woroch Paper").

only a diminishing effect.[21] Although several CLECs here have argued, based largely on Professor Jonathan Baker's regression analyses, that a building with special access demand should not be considered competitive unless *three* CLECs have built connections to that building, Professor Baker himself has filed a supplemental report which makes clear that his regressions do not support any such theory.[22] For all of these reasons, the precedent and the evidence support only one conclusion: there is no basis to adopt pricing flexibility triggers that in some way require a showing of more than one facilities-based competitor.[23]

3. Cable Company Offerings. The Commission asked whether AT&T views cable HFC-based services as a viable option when purchasing dedicated access outside of AT&T's ILEC footprint. The answer is yes. AT&T currently has contracts with **[BEGIN HIGHLY CONFIDENTIAL]** [redacted]

[21] Declaration of Mark Israel, Daniel Rubinfeld, and Glenn Woroch, *Special Access Rates for Price Cap Local Exchange Carriers*, WC Docket No. 05-25, RM-10593 (Feb. 19, 2016) ("Israel-Rubinfeld-Woroch Decl."), at 13-14, attached to Reply Comments of AT&T Inc., *Special Access Rates for Price Cap Local Exchange Carriers*, WC Docket No. 05-25, RM-10593 (Feb. 19, 2016) ("AT&T Reply").

[22] Supplemental Reply Declaration of Jonathan B. Baker on Market Power in the Provision of Dedicated (Special Access) Services, *Special Access Rates for Price Cap Local Exchange Carriers; AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Service*, WC Docket No. 05-25; RM-10593, at ¶ 7 (filed March 2, 2016) ("Baker Supplemental Reply") (acknowledging the magnitude of the coefficients in his analysis is not "precis[e]" and that **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]**); *see also id.* ¶ 7 n.12 (statement in original Baker declaration about third CLEC "lead[ing]" to the greatest ILEC price decrease **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]**).

[23] In all events, there are almost always two or more competitors for virtually all special access demand once one counts cable offerings (including HFC-based offerings), which, as explained below, the Commission should do.

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The marketplace for dedicated services has changed dramatically in recent years. In 2014 and 2015, AT&T conducted a comprehensive review of its approach to purchasing dedicated services outside of its ILEC wireline footprint. As part of that comprehensive review, AT&T implemented new initiatives that include, among other things, **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]**

AT&T has certified both fiber-based and HFC-based Ethernet offerings from cable companies for use in AT&T's flagship VPN and MIS services, as well as for use in AT&T's backhaul services. **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]**

During the meeting with Commission Staff, AT&T reiterated that it also faces intense competition from cable companies for retail special access customers within its ILEC footprint. As AT&T has previously explained, when a customer cancels an AT&T DS1 special access service in favor of a competitive offering, AT&T's sales team attempts to determine the competitor to which the customer switched.[24] Those data show that, for the thirteen-month period from November 2014 through November 2015, more than a **[BEGIN HIGHLY**

[24] AT&T Reply, at 26-27.

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CONFIDENTIAL] [redacted] **[END HIGHLY CONFIDENTIAL]** of AT&T's competitive losses were to cable companies and those losses are divided among cable fiber and HFC-based services.[25]

AT&T also reiterated during the meeting that AT&T is actively responding to competition from cable HFC-based services, including in the development of the next-generation Ethernet products and services that will replace legacy TDM-based DSn services. As just one example, **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]**

The CLECs' submissions also confirm that cable HFC-based services are competing against TDM-based and Ethernet special access services. For example, XO's Director of Product Analytics admits that XO is "regularly competing" against cable companies for small and medium sized businesses, that it "loses" small and medium-sized customers "to [cable] companies offering Best Efforts Internet," and that it has developed "products to this group of customers."[26] Similarly, Windstream's website advertises its "Ethernet Internet" service (with a 99.99% uptime guarantee) as a substitute for best efforts cable.[27] These CLECs clearly view cable "best efforts" services as a direct competitor to other business services with service level agreements. And cable companies, with their near ubiquitous networks, are especially well positioned to compete for much of the existing and very substantial growth in demand for data by businesses.[28]

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[25] *See id.*

[26] Declaration of James A. Anderson, ¶ 33, attached to the XO Comments.

[27] *See* Windstream, "Ethernet Internet," http://www.windstreambusiness.com/products/enterprise-network-services/dedicated-internet-services/ethernet-internet (directly comparing Windstream's Ethernet Internet service to "cable Internet").

[28] TDS has likewise previously explained that small businesses with 10 or fewer employees comprise more than 75% of its market and that many of these same customers "have different needs than larger companies and at time compromise on their preference for reliable and secure service by downgrading to best efforts broadband internet access service [presumably supplied by cable companies] for cost savings." Ex Parte Letter from Thomas Jones (TDS) to Marlene H.

Notwithstanding their own admissions and advertising materials, the CLECs have argued that HFC-based "best efforts" services lack the capability to provide multi-site services and service level guarantees, and thus are not viewed as substitutes for ILEC special access services which do have those features. This argument fails on multiple levels. Most fundamentally, as shown above, the record establishes that ILECs and CLECs are in fact losing a significant number of customers to HFC-based "best efforts" services. As the economic testimony makes clear,[29] service level guarantees and multi-site capabilities are just two factors that special access customers consider. Customers also consider, for example, price and speed. That is why AT&T offers a range of special access services with different combinations of price, speed, service levels, and other features. The cable company best efforts offerings are clearly viewed by many customers as having a combination of price, quality, speed, and other factors that make them a better fit than other services currently offered by ILECs or CLECs.

It should not be surprising that, in many cases, special access customers would view a 100 Mbps or faster best efforts service as a superior substitute for a guaranteed 1.5 Mbps service. The CLECs' dismissal of cable's broadband Internet product as a viable competitor to special access requires one to believe that the cable companies' 100 Mbps service may sometimes offer speeds that fall below the 1.5 Mbps service, or that such services would be subject to frequent and sustained outages. That is essentially absurd, and indeed, under most consumer protection statutes and the Commission's net neutrality rules, the cable companies could not lawfully offer a 100 Mbps service that in practice was comparable to only a 1.5 Mbps service. Furthermore, AT&T's analyses indicate that business demand for ordinary broadband Internet services (*i.e.*, services with less robust service level guarantees) is currently more than **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** of the marketplace in terms of revenues and is expected to increase. These data confirm that a very substantial portion of the special access marketplace will continue to require lower service level guarantees, such as those offered by many best efforts cable HFC services.

But even if (contrary to the evidence) there were some legitimate basis for finding that best efforts services do not compete for ILEC special access services, the cable companies' HFC facilities still cannot be ignored in any legitimate analysis of competition in the special access marketplace, because cable companies also offer other services using those facilities that do have multi-site capabilities and service level guarantees. Specifically, cable companies today offer

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Dortch (FCC), WC Docket No. 05-25 (Mar. 26, 2015), Butman Decl. at ¶¶ 5, 15. These statements strongly indicate that TDS is competing with the cable companies for 75% of its customer base.

[29] *See, e.g.*, Israel-Rubinfeld-Woroch Decl., ¶ 61; AT&T Reply, at 24-26.

HFC-based Ethernet services that can connect multiple sites and that include service level guarantees. TWC, in its March 3, 2016 *ex parte*, explained that it offers both multiple service sites and service level guarantees to its HFC customers:

> Ethernet service . . . can also be delivered over DOCSIS [HFC] or fiber. Subject to the unique requirements of each business, Ethernet service, *which connects a business across multiple locations*, is sold independent of the underlying technology delivering the services. As with [its Best Efforts] service, TWC's fiber Ethernet service delivers **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** At the end of 2015, in response to customer demands, TWC introduced SLAs for its Ethernet-over-DOCSIS service, and has since seen **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]**

Other examples include Comcast's Ethernet@Home, which is delivered over HFC, is backed by SLAs, and is available for a variety of Ethernet services at symmetric bandwidth speeds up to 10 Mbps.[31] In addition, Cox states that its Ethernet over HFC service allows customers to "extend the reach of [their] LAN to multiple locations.,"[32] and that its business services are backed by "industry-leading SLAs," which demonstrate its "commitment to providing . . . the highest level of service and support."[33] Cox also offers "Coax Ethernet" that supports "multi-point-multipoint" services.[34]

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[30] Time Warner Cable Inc. Notice of Ex Parte Presentation, *Special Access Rates for Price Cap Local Exchange Carriers*, WC Docket No. 05-25, at 2-3 (filed Mar. 3, 2016) (emphases added).

[31] Cindy Whelan, Current Analysis, Comcast Takes Telework to the Next Level with Ethernet @Home, at 2 (Dec. 16, 2014).

[32] Cox Metro Ethernet – HFC, Extend you LAN with Ehternet Simplicity over our extensive Hybrid Fiber Coax (HFC) networks, http://www.coxbusiness.com/meet/oc/sheila/pdfs/Metro%20Ethernet%20-%20HFC.pdf (last visited Mar. 15, 2016).

[33] Cox Business, *Reliable, Secure, High-Speed Business Internet*, https://www.cox.com/wcm/en/business/datasheet/ds-business-internet.pdf?campcode=xl_data_0908.

[34] Spectrum Business, *Ethernet*, https://business.spectrum.com/content/business-ethernet#coax.

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Lastly, Commission Staff asked whether there is merit to arguments that it should discount the availability of Ethernet over HFC with service level guarantees on the grounds that they are relatively new offerings and are not yet ubiquitous. The answer is no. If anything, the Commission should place *greater* weight on the existence of these offerings, because the Commission's regulation should be forward-looking and should allow for trends like Ethernet over HFC that clearly are taking hold and are already making an impact.[35]

4. **Lateral Extensions.** The record establishes that in areas where CLECs have deployed fiber facilities, the CLECs routinely compete for customers in buildings near their existing fiber networks, and deploy "lateral extensions" from their fiber networks to those buildings. Commission Staff indicated that it is continuing to evaluate how far CLECs can extend laterals from their fiber networks, and Commission Staff asked about the distances AT&T typically extends its fiber facilities.

AT&T's engineering guidelines demonstrate that AT&T engineers its network to maintain lateral distances at or below about **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** But the Commission need not rely on AT&T's data to evaluate how far CLECs are willing to extend laterals. The CLECs have submitted declarations that show that they typically deploy laterals ranging from **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** For example, as explained by XO's Vice President of Access Management and Implementation, as "a rule of thumb" XO will compete for customers and build laterals to buildings that are within **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]**

[35] *See, e.g., Comcast Corp.* v. *FCC*, 579 F.3d 1, 6-7 (D.C. Cir. 2009).

[36] **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]**

linear feet of its fiber facilities.[37] Similarly, Windstream explains that it extends fiber to buildings that are within **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** miles of its fiber facilities and that **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]**[38]

Given the general consensus in the record that CLECs can and do extend laterals ranging from about **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** it is clear from the record that CLECs can and do compete for virtually all special demand, because competitive facilities exist in just about every MSA census block with special access demand and those census blocks tend to be small. As explained by Professors Israel, Rubinfeld, and Woroch, the Commission's 2013 special access data show that competitive facilities exist in almost every **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** MSA census block with special access demand, and that those census blocks cover virtually all **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** of business establishments.[39] As explained by Professors Israel, Rubinfeld and Woroch, "[t]he median area of all MSA census blocks for which competitive providers reported a special access location is **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** square miles, while the mean size is **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** square miles."[40]

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[37] Declaration of George Kuzmanovski ¶ 24 ("Kuzmanovski Decl."), attached to the XO Comments. *See also* Declaration of Michael Chambless ¶ 26 ("Chambless Decl."), attached to the XO Comments (XO builds out to buildings within **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** feet of its facilities).

[38] Declaration of Dan Deem, Douglas Derstine, Mike Kozlowski, Arthur Nichols, Joe Scattareggia, and Drew Smith ¶ 51, attached as Attachment A to the Windstream Comments. Similarly, TDS has explained that "[o]ne way to get over the fiber build expense . . . was to pre-build routes along streets in a community near buildings with a particular focus on multi-tenant units," and to enter into master building entrance agreements that provided TDS access to these buildings. Sean Buckley, *TDS takes three-pronged approach to lighting business fiber*, FierceWireless (May 12, 2015), *available at* http://www.fiercetelecom.com/story/tds-takes-three-pronged-approach-lighting-business-fiber/2015-05-12?utm_campaign=AddThis&utm_medium=AddThis&utm_source=email#.VXBs6aqx2TM.email.

[39] Israel-Rubinfeld-Woroch Paper, at 5.

[40] *Id*. at 11. *See also id.* ("The mean size of a census block with special access service is skewed by a small percentage of very large census blocks in remote portions of MSAs. For instance, 75 percent of the metropolitan census blocks with special access service have an area less than

There is no contrary evidence in the record to support the CLEC claims that their fiber facilities are generally too far away from buildings with special access demand to justify extending a lateral if they win a customer in those buildings. Nor would any such claims be credible. It would require the Commission to believe that CLECs have deployed fiber facilities to nowhere, when in fact the CLECs' own declarants state that their practice is to deploy facilities near locations with special access demand, and then compete for customers and extend laterals to the buildings where they win customers.

To the extent the Commission determines that there is still an open issue of fact as to whether CLEC facilities are within striking distance of most special access demand, the Commission should make the fiber-based maps it collected, but has not released, available to interested parties (subject to the existing Protective Orders) so that parties can compute the actual distances from CLEC fiber facilities to the locations with special access demand. AT&T recently filed a motion seeking access to the fiber maps for precisely this purpose.[41]

5. **Analysis of Pricing**. The Commission also asked why the ILECs did not submit an analysis of how special access pricing responds to competition. Simply put, the data collection does not facilitate any reliable analysis of pricing. The data collection does not contain data on "prices." Rather, it contains data on revenue. Much of that data is missing: as Professors Israel, Rubinfeld, and Woroch have explained, **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** of all buildings in the FCC's dataset lack any billing data, and those omissions are not randomly distributed throughout the sample. In addition, different providers used different methods to report their revenues, which makes apples-to-apples comparisons difficult. Even if one could correct for these deficiencies, an analyst would still have to construct a measure of pricing by choosing a method of calculating revenues per "units" – another process that would require a variety of judgment calls and which could be done a number of ways.[42] As explained by Dr. Ford, "[a]lthough [the

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[BEGIN HIGHLY CONFIDENTIAL] [redacted] **[END HIGHLY CONFIDENTIAL]** square miles which is in the range of about half of the mean size. Consequently, the median size of a census block better reflects that 'average' than the mean size for these data.").

[41] *See* Motion of AT&T Inc. To Make Fiber Maps Available, *Special Access Rates for Price Cap Local Exchange Carriers*, WC Docket No. 05-25, RM-10593 (Mar. 17, 2016).

[42] For example, Professor Baker's description of his price variable suggests he relied on an internally inconsistent methodology to generate prices. He notes that he removed non-recurring charges from the "total_billed" variable in the pricing data but included out-of-cycle adjustments or discounts, even though the Commission in its "Instructions for Data Collection for Special

Commission's 2013] data may prove very useful in revealing the presence of competition in the sector, these data are not well-suited for much else. . . . In light of the OMB-mandated revision to the data request, which limited pricing information to a single year (2013), the analysis of prices will be much more limited and cursory than the Commission originally intended."[43]

The one attempt to perform such a pricing analysis in this record – the regression analyses performed by Professor Jonathan Baker – illustrates the futility of trying to use the data collection to model special access pricing. Professor Baker tried to model the effect of CLEC entry on ILEC special access prices on a building-by-building basis, but the results are useless for any purpose in this proceeding. Professor Baker concedes that his estimations are statistically biased (and he made no further effort to correct the bias); most of the results he chose to report are either statistically insignificant or directly contrary to his predictions; and in all events the pricing effects he estimates are so small they would be *practically* insignificant even if they were statistically significant.[44] Professor Baker's failed attempts confirm that it is highly unlikely that the data collection can provide any worthwhile insight into special access prices.

To be sure, the Commission's original vision in the Notice of Proposed Rulemaking was to perform a "one-time, multi-faceted market analysis," one element of which would have been "panel regressions" seeking to determine marketplace factors that affect special access pricing.[45] That original vision, of course, was based on the assumption that the Commission would collect data from two different years, which would have allowed the Commission to run regressions to estimate the change in prices over time as entry occurred. In the end, however, the Commission collected data from only a single year (2013), and even so, the Commission had always maintained that "the precise form of econometric modeling we conduct will be dependent, in large part, on the nature and the quality of the data produced in response to the Order."[46] As it turns out, the "nature and the quality" of the single year of data in the actual data collection do

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Access Proceeding" described out-of-cycle adjustments and discounts as payments or revenues that are not billed on a recurring basis. Israel-Rubinfeld-Woroch Decl. ¶ 28 n.21.

[43] George S. Ford, The Road to Nowhere: Regulatory Implications of the FCC's Special Access Data Request, Perspectives, Phoenix Center for Advanced Legal & Economic Public Policy Studies (Feb. 23, 2016), *available at* http://www.phoenix-center.org/perspectives/Perspective16-02Final.pdf.

[44] *See, e.g.*, Israel-Rubinfeld-Woroch Decl. ¶¶ 18-42.

[45] Report and Order and Further Notice of Proposed Rulemaking, *Special Access for Price Cap Local Exchange Carriers*, 27 FCC Rcd. 16318, at ¶¶ 66-68 (2012).

[46] *Id.* ¶ 68.

not lend themselves to any robust analysis of pricing. Given the inadequate amount of time the Commission gave the parties for analysis and the severe challenges of attempting to use these data to construct any meaningful estimation of pricing effects, AT&T and the ILEC economic experts focused their attention on the primary questions raised in Part IV.B of the NPRM, which relate to the extent to which ILECs face facilities-based competition (which, by its nature, ensures just and reasonable rates).

6. Conduit. Commission staff asked FCC asked whether CLECs actually have regulated access to ILEC conduits. They do. Under Sections 224 and 251(b)(4), ILECs are required to provide nondiscriminatory access to conduit space to buildings at rates regulated under federal law.[47]

7. Proposed Action. Finally, the Commission asked what action it should take in response to the comments. As AT&T has previously explained, there is no basis in the record to revisit any grant of Phase II pricing flexibility. With respect to services in MSAs that are still subject to Phase I relief or "no relief," the Commission must devise mechanisms by which ILECs like AT&T can obtain Phase II level relief where the data show that AT&T is subject to facilities-based competition. The need for new Phase II triggers is long overdue, as the data confirm that the largest cities in the AT&T region, like Chicago and Dallas, are among the most intensely competitive special access marketplaces in the country and yet still have only Phase I relief for channel terminations. The Commission can and should provide that relief in two ways: (1) it should simply grant relief for the largest MSAs immediately in this rulemaking;[48] and (2) it should use the data collection to adjust the triggers to reduce the under-inclusiveness of the Phase II relief. As AT&T has previously noted, it is not in a position at this time to recommend any particular adjustment because it has not had sufficient time to test alternative triggers against the data to determine an alternative trigger that most appropriately addresses the under-inclusivity of the triggers. But any such change should either relax the collocation requirements and/or establish an alternative, additional path by which ILECs may gain Phase II relief in geographically smaller areas (such as downtown areas and other business districts), if such

[47] 47 U.S.C. ¶¶ 224, 251(b)(4); *see also* Memorandum Opinion and Order, *Petition of USTelecom for Forbearance Pursuant to 47 U.S.C. § 160(c) from Enforcement of Obsolete ILEC Legacy Regulations That Inhibit Deployment of Next-Generation Networks, et al.*, WC Docket No. 14-192, et al., 2015 FCC LEXIS 4006 (December 28, 2015), at ¶¶ 79-84 (granting forbearance from these requirements for *new builds* (*i.e.*, greenfield locations) but not for existing locations).

[48] Comments of AT&T, *Special Access Rates for Price Cap Local Exchange Carriers*, WC Docket No. 05-25, RM-10593, at 23-26 (Jan. 27, 2016).

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geographically granular relief can be practicably administered and implemented without unnecessary cost or complexity that is confusing for ILECs or their customers.

Sincerely,

/s/ Christopher T. Shenk
Christopher T. Shenk
Attorney for AT&T Inc.

Attachments

cc: Christopher Koves

ATTACHMENT A

Special Access for Price Cap Local Exchange Carriers

WC Docket No. 05-25

AT&T

March 2016

Summary

- The 2013 data show that in Phase II MSAs, competitors have deployed fiber in almost every census block with special access demand, and that those census blocks cover virtually every business establishment.
- The 2013 data show that the same is true for many Phase I and "no relief" MSAs.
- The 2013 data thus confirm that there is no basis for rolling back Phase II pricing flexibility in any MSA, and that the Commission should immediately extend Phase II pricing flexibility to many Phase I and "no relief" MSAs.
- The 2013 data further confirm that, going forward, the Commission should relax the Phase II triggers, and explore administratively feasible methods to promote Phase II relief on more granular levels.
- The analyses submitted by the CLEC economists are fundamentally flawed because, among other things, they: (1) ignore nearby fiber facilities; (2) ignore cable competition (including *all* HFC-based competition); (3) are based on incomplete data; and (4) produce clearly absurd results.

The 2013 Data Confirm that the Pricing Flexibility Triggers Are Underinclusive

- For Each Phase II MSA, the Compass Report shows:
  - Competitive facilities are in virtually every census block;
  - These census blocks contain virtually every business establishment;
  - These census blocks are small, such that the competitive facilities in these census blocks can generally reach all or most buildings.
  - The same results are found even if a significant portion of cable facilities are excluded, including all HFC facilities.

- These results are found in many Phase I and "no relief" MSAs, confirming that the triggers are *under*inclusive.

The Record Confirms That The FCC Should Maintain And Expand Phase II Relief

- The FCC should retain all existing Phase II MSAs.
  - The data confirm that the triggers have provided Phase II relief to MSAs with wide-spread competitive facilities.
- The FCC should extend Phase II relief to Phase I and "no relief" MSAs where the data show substantial competitive facilities.
- Going forward, the triggers should be revised to better reflect the presence of competition:
  - *e.g.*, by maintaining the existing MSA approach with liberalized triggers
  - *e.g.*, by supplementing the MSA approach with an additional means of gaining relief on a more granular basis (such as on the zip code or census block level)
- Any revision to the current regime based on more granular geographic areas must be reciprocal, *i.e.*, must provide regulatory relief for ILECs where competition is present (like, for example, in downtown Chicago)

The CLECs' Requested Relief Would Be Unworkable and Unlawful

- Re-imposition of price caps in relatively demand-empty census blocks on the outskirts of MSAs with Phase II relief would make no sense and provide no meaningful benefits
- CLECs have offered no evidence in either the data collection or otherwise that would support reinitialization of the price caps
- Any attempt to calculate a new X-Factor would require years of deliberations and would likely be reversed
- There is no basis for revisiting forbearance for Ethernet services:
  - Ethernet services are not subject to this proceeding; and
  - The data collection and the record more generally confirm that ILECs, CLECs, and cable companies are all competing successfully to provide Ethernet.

The CLECs' Analyses of the 2013 Data Are Fundamentally Flawed

- The CLECs submitted two studies of the 2013 Data:
  - Besen/Mitchell Study: relies on historic market shares, based solely on building connections.
  - Baker Regression: attempts to measure whether ILEC prices change in response to the number of CLECs that have connected to a building or that have deployed facilities nearby to a building.

The Besen/Mitchell Study Fails To Account for Nearby Competitive Fiber Facilities

- Failing to account for nearby fiber ignores how competition occurs in the marketplace:
  - When competitors enter the special access marketplace, they deploy facilities (often fiber rings) in business districts
  - These competitors then market dedicated services to businesses located in those business districts
  - When a competitor wins a customer, the competitor extends its facilities to the customer's building
  - ILECs thus compete against competitors that have deployed facilities in the same area, regardless of whether the CLEC has already extended its facilities to a particular building
- The CLECs' own testimony confirms that they compete to serve buildings at significant distances from their fiber facilities
- Even Professor Baker – an economist hired by the CLECs – attempts to account for the impact of nearby fiber

It Is Obviously Economically Feasible To Extend Laterals

- CLECs argue that they often cannot compete for customers in buildings to which they have not yet connected.
  - The CLECs own declarations show that their entire business plan is to deploy fiber rings, compete for customers, and then connect those customers to the fiber rings.
  - If the CLECs are to be believed, they deployed fiber facilities throughout areas with special access demand, but have no plans to actually compete for customers using those facilities.
- The FCC found that it is reasonable to impose a merger condition on AT&T/DirecTV that required fiber to be expanded to *12.5 million* new residences. If it is truly economically infeasible to deploy fiber laterals, the FCC could not defend such a condition (and AT&T would not have agreed to it).
- The Courts, the DOJ, and the FCC have all in the past concluded that nearby fiber must be counted
  - *WorldCom*, 238 F.3d at 458 ("the presence of substantial sunk investment, and the resulting potential for entry into the market, can limit anticompetitive behavior by LECs")
  - *AT&T Inc. and BellSouth Corp.*, 22 FCC Rcd. 5662 ¶¶ 42-49

The CLECs' Claimed Technical Impediments Are Invalid

- No merit to CLEC assertion that their transport facilities cannot be used to serve customers:
  - These claims are based on legacy architecture that is no longer commonly used
  - Today, with single-mode fiber any part of a fiber ring can provide both transport and service
- No merit to CLECs assertions that their fiber rings may lack sufficient capacity to serve every building passed
  - Expanding capacity of fiber requires only upgrades to optical equipment, not additional fiber deployment
- No merit to claims that CLECs nodes are too far away to serve potential customers
  - No provider would reasonably deploy fiber facilities in an area without also including a sufficient number of access points to serve the businesses passed by the fiber facilities
  - AT&T designs its fiber architecture with nodes at intervals that ensure that it can serve nearby customers
- No merit to CLEC claims that trenching is too expensive - they have regulated access to ILEC conduit and poles

The Besen/Mitchell Analysis Fails to Account For Cable Facilities

- FCC decided not to require cable companies to provide information on their Hybrid Fiber-Coaxial ("HFC") facilities because that data is already available as part of the National Broadband Map ("NBM")
- The Besen Mitchell study failed to include the NBM HFC data
- The Besen Mitchell study also failed to supplement the special access data with additional fiber-based cable facilities data, which were not included in the special access data submission but are available on the NBM
- By contrast, the Compass Lexecon Study appropriately supplemented the FCC's 2013 special access data collection with 2013 cable company data collected by the FCC and NTIA as part of the National Broadband Plan

There Is No Legitimate Basis For Ignoring Competition From Cable Companies

- The CLECs concede that cable's fiber-based services compete against ILEC special access services
  - Nonetheless, the Besen Mitchell Study makes no attempt to supplement the 2013 data with such data from the NBM
- The CLECs argue that cable HFC business services should be ignored because
  - HFC services cannot support multi-location services; and
  - HFC services cannot offer service level guarantees similar to those offered by special access services.
- The record shows that every step of this argument is incorrect.

It Is Not True That Cable's HFC Business Services Are Not Substitutes for TDM Products

- Cable companies have explained that they also offer Ethernet services over their HFC facilities ("EoHFC")
- Cable companies have explained that these Ethernet services are capable of offering multi-location services
- Cable companies have explained that they also offer Ethernet services over HFC with symmetrical speeds and service level agreements comparable to those offered by ILECs and CLECs
- Conclusion: Cable companies offer direct substitutes for ILEC special access services over their HFC facilities

No Merit To Claims That Cable HFC Services and Special Access Services Do Not Compete

- The CLECs assert that special access customers demand service level guarantees that are not available from cable HFC business services.
- This assertion is refuted by the fact that ILECs and CLECs are losing special access customers to cable companies' HFC services and taking steps to respond to that competition.
  - In fact, customers consider the combination of price, service levels, and other factors when purchasing dedicated services.
  - For some customers, price is the more important, and they are willing to give up service level guarantees in return for lower prices.
  - This is why AT&T offers a wide range of prices and corresponding service level guarantees with its TDM and Ethernet products.
- In any case, the CLEC assertion that no customer views a 100 Mbps best efforts cable as a better alternative to a 1.5 Mbps DS1 or to a 45 Mbps DS3 product is simply not credible.
  - The 100 Mbps cable best efforts connection is much faster
  - The 100 Mbps can be much less expensive.

The Flawed Baker Regressions

- Prof. Baker posits that ILECs have market power if it can be shown that ILECs reduce prices when CLECs enter, either by connecting to buildings previously served only by an ILEC, or by deploying facilities in the vicinity of such buildings
- Prof. Baker claims that his regression analysis shows a statistically negative correlation between ILEC prices and CLEC entry, thus confirming his hypothesis that ILECs have market power
- In fact, Prof. Baker's Regressions:
  - Say nothing about competition in Phase II areas, and thus cannot be used to evaluate the competitive triggers (the central issue in this proceeding).
  - Do not in fact show a consistent negative relationship between ILEC prices and CLEC entry;
  - Are based on incomplete data and are misspecified;
  - Are biased, even according to Prof. Baker.

The Baker Regression Says Nothing About The Competitive Triggers

- The central issue in this proceeding is whether the FCC's competitive triggers for Phase II pricing flexibility are under- or over-inclusive.
  - But, Prof. Baker does not even present a regression for Phase II areas
  - Indeed, Prof. Baker admits that he failed to find *any evidence* of a consistent negative relationship between price and the number of competitors in Phase II areas
  - This indicates that ILECs lack market power in those areas, and that, therefore, the existing triggers are valid
- Conclusion: The Baker regressions fail to address the central issue in this proceeding

The Baker Regression Does Not Establish A Consistent Negative Relationship

- Prof. Baker ran 13 regressions, producing 91 coefficients (1st, 2nd, 3rd CLEC connection to a building; and 1st, 2nd, 3rd, and 4th CLEC nearby fiber deployment).
- More than half of the coefficients were NOT statistically significant.
- Of the remaining coefficients, several showed a positive, not negative correlation.
- Professor Baker admits that even more coefficients may be statistically insignificant (and that more would be positive and statistically significant), if he used a different, and possibly more appropriate, method for computing standard error.

The Baker Regression Produces Absurd Results And Is Biased

- The regression produces many facially absurd results, which indicate that it is flawed. Examples include:
  - The regressions indicate statistically significant impact on ILEC prices only after the 3rd CLEC connects to a building.
  - The regression has statistically significant results indicating that CLECs increase prices as more CLECs connect to a building.
  - The regression indicates that CLEC fiber facilities located nearby a building can have a greater impact on ILEC prices that CLECs actually connected to the building.
- Prof. Baker himself admits that his regression is biased
  - Professor Baker hypothesizes that all of the biases in his analysis understates the actual extent to which the coefficients are negative. But he provides no analysis of testing.
  - The Compass Lexecon economists have shown that there are multiple reasons why Prof . Baker's analyses are, in fact, biased in the other direction (*i.e.*, they overstate negative relationship)

The Baker Regression Analysis Is Based On Incomplete Data

- Prof. Baker's regression compares ILEC prices to the number of competitors at or near to a building.
- But his regression is missing substantial data for both metrics.
  - Missing prices: The regression is based on data that is missing prices for a substantial portion of the locations in his analysis.
  - Missing Competitors: The regression is based on data with an incorrect number of competitor connections at many locations
  - The 2013 Special Access data is missing location information for more than 100,000 connections
  - The regression excludes all cable company HFC (and a substantial portion of cable Fiber-based) connections.

Questions?

ATTACHMENT B

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]